



National Biodiesel Board
P O Box 104898
Jefferson City, MO
65110-4898
(573) 635-3893 *ph*
(800) 841-5849
(573) 635-7913 *fax*
www.biodiesel.org

ISSUE BRIEF

Biodiesel Tax Credit Implementation

To date, the IRS has issued two guidance documents relative to the volumetric biodiesel credit passed as part of the JOBS Act of 2004. The two Notices are:

1. IRS Notice 2005-04
2. IRS Notice 2005-62

These documents can be found on the IRS website at www.irs.gov and on the NBB website at www.biodiesel.org.

The IRS guidance documents (IRS Notice 2005-04; IRS Notice 2005-62) are the only official documents that can be conclusively relied upon until a later guidance document is issued. This issue brief is NBB's interpretation of those documents to help clarify certain basic issues based on discussions by the IRS-Biodiesel Industry task force.

This issue brief should not be construed by anyone as offering tax advice. NBB will continue to reiterate to entities intending to claim the excise tax credit or the income tax credit that they should seek the services of a qualified tax professional.

1. Effective Dates

- The income and excise tax credits provided for biodiesel/agri-biodiesel in the JOBS Act of 2004 became effective January 1, 2005 and are set to expire December 31, 2008 (per an extension provided for in the Energy Policy Act of 2005).

2. Biodiesel Producer, Importer, and Blender Registration

- Biodiesel producers or importers of biodiesel must register with the IRS and have their application approved by the IRS prior to commencing production. The application and approval process may be a lengthy process. Applicants should contact the IRS to determine how much lead time is involved in the application approval process.
- Application for registration is to be done via IRS Form 637. The Service has updated its Form 637 and has developed two (2) new Activity Letters under which a producer/importer will register as either one or both depending on whether they produce "biodiesel" and/or "agri-biodiesel". The updated Form 637 is available on the *Forms and Publications* page of the IRS website: www.irs.gov.
 - a. The new Activity Letters are: "AB" for producers and importers of agri-biodiesel; and "NB" for producers and importers of biodiesel (other than agri-biodiesel).

- Companies who are both: biodiesel producers and blenders of biodiesel/agri-biodiesel into diesel fuel will have a combination of Activity Letters on their Form 637 registration that denotes production and blending.
- Blenders must receive a 637 M designation from the IRS by applying for it on Form 637.
 - a. Existing “T” registrants who are blenders must be re-registered using Activity Letter “M”.
 - b. Entities that are not currently blenders, but wish to do so must register with the IRS as an “M” registrant.
 - c. Blenders must have their application approved by the Service prior to commencing any blending activity.
 - d. The application and approval process may be a lengthy process. Applicants should contact the IRS to determine how much lead time is involved in the application approval process.

3. Certificate For Biodiesel

- The JOBS Act states that a biodiesel mixture credit is not allowed unless the producer of the mixture (i.e. blender) obtains a certificate from the biodiesel producer that identifies the product as “biodiesel” or “agri-biodiesel”, that it is properly registered as a fuel with the EPA and that it meets the requirements of ASTM D 6751.
- Due to time constraints *IRS Notice 2005-04*, published in December 2004 does not provide guidance for all of the various distribution and inventory storage scenarios that may be encountered.
 - a. This Notice provides a model *Certificate for Biodiesel* to be utilized until further guidance is provided.
 - b. In making a claim to the Service for credits and/or refund, the claiming entity must have the necessary certificates in hand prior to making a claim.
 1. The claimant should retain the certificate as a part of their business records in support of the claim.
- *IRS Notice 2005-62* revises the certificate to clarify that the claimant may obtain the certificate either directly from the producer of the biodiesel or indirectly from a biodiesel reseller. This was done in an effort to address the various distribution scenarios encountered by industry.
 - a. This Notice provides specific detail regarding “re-seller” certificates and the requirements surrounding their use.
- *IRS Notice 2005-62* included further revision that the claimant generally must submit a copy of the certificate with their claim.

4. Claiming Credits & Receiving Payment for Excess Credits

- The definition of a “mixture” as it applies to the “mixture credit”. *IRS Notice 2005-62* clarified that a “biodiesel mixture” is a mixture of biodiesel and diesel fuel containing at least 0.1 percent (by volume) of diesel fuel. Thus, for example, a mixture of 999 gallons of biodiesel and 1 gallon of diesel fuel is a biodiesel mixture.
- Eligible entities are currently able to file claims with the Service for credits and/or payments. Claimants must follow the procedures outlined in *Notice 2005-04* and *Notice 2005-62* which include the following mandatory steps:

- a. Blenders must use Form 720, Quarterly Federal Excise Tax Form; and Form 8849 to claim their credit(s) and payment for the excess sum of their credit(s) above their excise tax liability.
 - b. Blenders must use Form 4136, Credit for Federal Tax Paid on Fuels; or Form 8846 Biodiesel Fuels Credit when claiming an income tax credit.
- Receiving payment for excess credits. Until additional guidance is given, payments will be issued to claimants making claims in accordance with the process as proscribed in *Notice 2005-04* and *Notice 2005-62*. Timing for payments is consistent to those outlined in the JOBS Act:
 - a. Within 45 days (paper claims) w/out interest accruing.
 - b. Within 20 days (electronic claims) w/out interest accruing.
- The IRS has updated both Form 720 and Form 8849 and their accompanying Schedules to reflect the inclusion of the biodiesel credit provisions of the JOBS Act.
 - a. The revised Forms and Schedules are now available on the *Forms and Publications* page of the IRS website at www.irs.gov.

5. Other Items of Understanding

- IRS Notice 2005-62 provided further clarification regarding the definition of “agri-biodiesel” to state the list of eligible feedstocks in the JOBS Act is not an exclusive list and that for example biodiesel derived solely from virgin oils includes esters derived from palm oil and fish oils.
- Heating Oil. Heating oil is considered a taxable fuel that is exempt from taxation. Because of this, blending biodiesel and agri-biodiesel into heating oil would be considered as an eligible activity upon which the blender could make a Biodiesel Mixture Credit claim.
- B100 used as a fuel. The IRS Notice 2005-04 addresses this in section 2 (e) on page 4. The guidance states that use of unblended B100 as a fuel qualifies for the income tax credit but not the excise tax credit. Entities should refer to Rev. Rul. 2002-76 for additional information regarding taxation of biodiesel. As is noted in that ruling, biodiesel is not included in the definition of a taxable diesel fuel (because it contains less than 4% normal paraffins). Tax is imposed on biodiesel when it is either a) blended into non-exempt taxable diesel fuel, or b) when B100 is delivered as fuel directly into the tank of a diesel-powered highway vehicle or a diesel-powered train. An entity that delivers B100 as a fuel directly into the tank of a vehicle may claim a nonrefundable income tax credit.
- It is important to note that entities that blend biodiesel into undyed diesel fuel MUST report and remit the 24.4 cent per gallon tax on Form 720. As mentioned previously, the claimant may claim the applicable credit against their tax liability. Failure to report and remit taxes could result in substantial penalties including fines and imprisonment.

6. Application of These “Understandings” to a Practical Scenario

- When a blender reports a tax liability (ie. blending into undyed diesel), it would utilize Form 720 reporting the gallons of biodiesel/agri-biodiesel blended, calculate the total tax, and claim the value of their Biodiesel Mixture Credits to offset their tax liability.

Claims requesting a refund of the excess value of Biodiesel Mixture Credits above a blender’s excise tax credit should be able to be made prior to the end of the quarter utilizing Form 8849.

- When a blender has no tax liability to report (ie. blending only into dyed diesel), it would utilize Form 8849 to make a claim for their excess biodiesel mixture credits.

IMPORTANT - Blending undyed biodiesel/agri-biodiesel into dyed diesel fuel:

- **Blenders must take necessary action to ensure the finished blend meets required federal dye concentration specifications. If not, the blended fuel would be subject to taxation.**
- **New fuel fraud provisions in Section 854(c) of the JOBS Act require that all dye added to diesel fuel must be added by tamper-proof, mechanical injection. This provision becomes effective 180 days after the final regulations are issued. Final and temporary regulations were issued on April 26, 2005 and become effective on October 24, 2005. The new regulations are clearly susceptible of an interpretation that they require the mechanical injection of dye only in cases of removals of diesel and kerosene from terminal racks and bulk transfer facilities. However in conversations with IRS Office of Chief Counsel, the regulations were not intended to be interpreted as applying only to dyeing at terminal racks or bulk transfer facilities. The IRS may well answer questions regarding whether, and under what circumstances, the mechanical dyeing requirements apply below the rack. Therefore to date, the applicability of this requirement below the rack remains an open question.**

General Example:

Producer P sells 1,000 gallons of agri-biodiesel to Blender B. P provides B with a certification of the fuel. B blends 400 gallons of the agri-biodiesel into dyed diesel fuel and 600 gallons into undyed fuel at various blend levels. B also adds dye to the dyed mixtures to maintain dye concentration requirements.

B carefully maintains consistent inventory records of incoming and outgoing volumes of biodiesel as well as the certifications on inventories in accordance with generally accepted accounting principles. B reports on Form 720 a tax liability of \$146.40 (600 gallons x \$.244). B also reports on Form 720 a total tax credit of \$147 (147 gallons of agri-biodiesel x \$1), enough to reduce B's tax liability to zero. B is able to claim a refund for the excess value of its credits (\$853) on Form 8849 prior to the end of the quarter [(400 gallons of agri-biodiesel blended into dyed diesel x \$1) + (453 gallons of agri-biodiesel blended into undyed diesel x \$1)].